ATLANTIC CANADA OPPORTUNITIES AGENCY

Audit Directorate

Review Services Division

Post Payment Audit Process
Status Report for Fiscal Years 2000/2001
and Recommendations for Process Improvement

FINAL REPORT

March 2002
(Audit 2002-002)

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Executive Summary

Results from the Post Payment Audit function for fiscal year 2000/01 showed that the payment process used by the Agency to verify claims from clients is currently working satisfactorily. The errors, discovered from the audits conducted, expressed as a rate for the entire claims processed for the year was 1.9% of the total dollar value of claims processed; which is well under the standard of 3%.

There were also improvements in the timeliness of the completion of the Post Payment Audits. For fiscal year 2000/01 the audits for the year were completed four months ahead of the previous fiscal year. This trend has continued in the current fiscal year with approximately 66% of the scheduled audits for the period April through October 2001 already completed.

An improvement was made in the distribution and recording of the results from the audits by the implementation of an Intranet website for the Post Payment Audit function. This interactive website allows for timely distribution of the claims being sampled and the results from the audits conducted.

There is a concern that the timeliness of the completion of the Post Payment Audits will not continue at a satisfactory rate. Advances, which require approximately six months before being eligible for audit, are representing an increasing portion of the claims being selected for audit. Currently advances represent 32% of the claims selected for audit, a significant increase from the representation of 22% in fiscal year 2000/01. We have recommended a review of the use of advances. We also recommend a review of the Post Payment Audit process to determine if there are opportunities to report on the completion of audits without waiting for the advances to be audited.

Observations and Recommendations

Sampling Levels

In order to formulate reliable conclusions on the soundness of the payment process, the Agency uses representative, statistical sampling to select claims for audit.

A sample of 265 claims, totalling $24.6 million was selected for fiscal year 2000-2001; representing 22% of the total dollar value paid by the Agency and 7% of the number of claims. This coverage is consistent with the previous fiscal year. The sampling methodology applied by Audit Directorate emphasizes large dollar value claims and addresses one of the major criteria of risk to the Agency.

As recommended in the 1999-2000 Status Report on Post Payment Audit, a full review of the approach to the statistical sampling procedure was undertaken in 2000-2001. An independent statistical sampling consultant reviewed the sample design, audit approach, and reporting system. The conclusion from the review was that the sample design was sound and results reported from the Post Payment Audit sampling were representative of the total population of payments made. A recommendation that the sampling interval and sampling level be adjusted was implemented immediately.

The independent review has confirmed that the sampling methodology and coverage will produce results suitable for conclusions to be drawn on the whole population of claims paid by the Agency.

Results from Post Payment Audits

When a Post Payment Audit is undertaken, the auditor compares the type of expenditure and amount claimed by the client to the terms and conditions of the contract, supporting documentation for eligible costs claimed, and other control aspects. If the auditor determines that an amount claimed by the client is inappropriate, an error is reported. These errors are accumulated throughout the year and the impact of these errors is expressed annually. The objective is to determine if the error rate is higher or lower than an established standard, which is the maximum error rate that can be tolerated in order to conclude that the Agency's payment process can be relied upon.

Error reporting is currently done by the extrapolation of errors found in the sampled payments over the entire population of payments made. (Previously, we reported the errors as a percentage of claims sampled.) This approach is designed to be conservative, ensuring that the maximum possible impact of identified errors is recognized. This method will give the Agency additional comfort that actual errors are within the established maximum.

An additional modification, which was implemented in fiscal year 2000/01, is the reporting of errors in two categories; *Processing Errors* and *Client Reporting Errors*. *Processing Errors* are errors which should have been caught by application of current Agency claim verification procedures. This situation indicates a breakdown of existing procedures, which can be addressed within the current payment system and are the responsibility of Agency management. *Client Reporting Errors* are instances where the on-site audit of documentation supporting claimed amounts shows that the documentation is insufficient to support a claimed amount. These errors could not be initially identified by the payment process currently employed.

An error rate of *Client Reporting* errors for the year, greater than the error rate standard, would indicate the need to review the current payment system to identify ways to eliminate or reduce the errors at the time the payment is received from the client.

The following table indicates the coverage and error rates for the fiscal year 2000-01.

Fiscal Year 2000/01

Item	Number of claims	Dollar Value	% of Dollar Value
Agency Total Claims Paid	3673	$11[illegible]481,988	N/A
Agency Total Claims Sampled	265	$24,616,776	22
Total Errors found by PPA*		$2,601,300	2.3
Processing Errors		$444,250	0.4
Client reporting errors		$2,150,050	1.9

*Expressed as an extrapolation over the Agency Total Claims Paid.

For the fiscal year ended March 31, 2001 we have concluded that the error rate is within the acceptable threshold if 3% for the Agency to rely on the payment process. (See Maximum Acceptable Error Rate on Page 5.)

Comparison with Previous Years

As a result of the change in reporting approach, the results for the current year are not directly comparable to the prior years. However, to provide a comparison, we have expressed the results in the same manner as the prior years.

The following tables indicate the annual results of Total Agency Errors Reported as a percentage of claims sampled for the last three fiscal years.

Fiscal Year 2000/2001

Agency Total Claims Paid	3673	$112,481,988	N/A	N/A
Agency Total Claims Sampled	265	$24,616,776	7	22
Total Agency Errors Reported	44	$419,707	17	Median of Range
				1.7

Fiscal Year 1999/00

Agency Total Claims Paid	4275	$127,069,817	N/A	N/A
Agency Total Claims Sampled	290	$28,972,929	7	22
Total Agency Errors Reported	37	$1,168,629	12	Median of Range
				4.0

Fiscal Year 1998/99

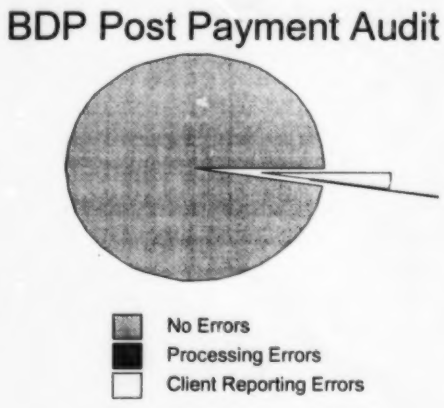
Agency Total Claims Paid	4579	$149,956,654	N/A	N/A
Agency Total Claims Sampled	406	$50,121,301	9	33
Total Agency Errors Reported	53	$1,465,163	13	Median of Range
				2.9

This data shows a significant drop in the median of range for the last fiscal year over the two previous years.

Maximum Acceptable Error Rate

The establishment of a maximum error rate has been a challenge. Organizations could not be identified which had a payment system or the added control feature of a Post Payment Audit regime, similar to the one employed by the Agency. The review of the statistical sampling process has provided confidence that the sampling approach is sound and that maximum error rates suggested by the Agency are appropriate.

The maximum error rate has been established as 3% of the total dollar value of the claims processed in the fiscal year.



A number of factors were considered in establishing the 3% standard:

a) private sector standards of 2% for direct expenditures;

b) the majority of payment errors are corrected by subsequent payments;

c) the policy that Agency assistance is repayable, thus ensuring that the majority of payment errors are subsequently repaid to the Agency.

Reporting Practices

Although the timeliness of reporting PPA results remains a concern, there has been improvement in the completion rate and timeliness of reporting. For fiscal year 2000-01, this effort has resulted in the ability to produce the status report four months earlier than the previous year. This strong effort has continued into fiscal year 2001/02. From the period April through October 2001, 67% of the sampled claims have been completed on schedule (See **Appendix B**).

The objective for the completion of the PPA audits is currently 90 days from the date of the sampled payment was provided to the regional office. We now have sufficient history of the Post Payment Audit process to conclude that this three-month standard is not achievable; primarily as a result of the use of advances. Advances add an average

of three months to the time required to complete Post Payment Audits, resulting in a six-month wait for the PPA results for affected sampled payments.

During the 2001/2002 year, a number of improvements were made to the reporting of PPA results. A Post Payment Audit Intranet site was established to improve the distribution of sampled claims to the regional offices and the streamlining of the reporting of the PPA audit. With the Intranet site now established, quarterly reporting for the fiscal year 2002/03 is practical.

Recommendation

That Audit Directorate report completion rates and the results from the audits on a quarterly basis, beginning with the fiscal year 2002/03. This quarterly report should include both Agency wide and regional based performance. The Annual Status Report will be prepared by Audit Directorate summarizing the year's performance, conclude on the appropriateness of the payment process (based on the results from the Post Payment Audits), and offer recommendations for improvement.

Policy and Procedures Manual

The policies and procedures for PPA were reviewed during 2000/01. Two additional sections were written to provide additional guidance to regional staff. The two new sections; "***Error Determination" and " Advances"*** were posted to the *Policy and Procedures* section on the Post Payment Audit Intranet site. Regional staff have access to the Intranet site and postings to the site trigger e-mail notification, ensuring staff are aware of updates.

Advances

Advances represent a significant number of the payments selected for Post Payment Audit. For the period April – October 2001, 32% of the payments selected are advances (See **Appendix C**). This is a significant increase from the 22% rate in fiscal year 2000-01 (See **Appendix D**).

Auditing an advance payment has been simplified and the guidance on the approach has been posted to the Post Payment Audit Intranet site. The approach was developed in consultation with the statistical consultant to ensure that the results would be statistically sound.

Advances significantly extend the time required to obtain sufficient information to complete the Post Payment Audit. We feel it is important that advances be reduced as much as possible, as indicated in the BDP Policy and Procedures manual. Advances should not be used where a progress payment or joint payment can be used and

Agency funds should not be advanced in advance of need. In the case of commercial clients, the cases where an advance payment will be required are rare. There will be a concern remaining on the non-commercial accounts where the need for advances is more apparent.

Recommendation

We recommend that all regional offices review the use of advance payments for the BDP and eliminate the use of advances where they are not made in accordance with the BDP Policy and Procedures manual. For commercial clients, we would expect that advance payment would be rare, as progress payments and joint payments should meet the needs of the client.

Processing Errors

Processing errors are errors which should have been caught by application of the current Agency claim verification procedures. Sufficient information was provided by the client on the claim which would have allowed the error to be identified. For 2000/01, the processing error rate represented $444,250 or 0.4% of the total population of payments made. It is important for regional management to understand how the current payment procedures broke down in the specific situation and how the problem might be prevented in the future. It is equally important for management to establish a threshold which governs the need for more monitoring of the payment process.

Recommendation

We recommend that in the cases of processing errors that regional management review the specific cases involved, identify how the error occurred, and take corrective action. We also recommend that a threshold be established which represents the maximum dollar value of Processing Errors which can be accepted by the Agency before the monitoring of the payment process needs to be enhanced.

APPENDIX A - Process Used to Sample Payments

The Agency employs a payment process which relies on the clients' personal attestation that expenses claimed are authentic, eligible costs of the project that have already been incurred. For claims of acceptable risk, this process is applied, and for claims of higher risk, the Agency can and does apply more strict claim verification procedures. In order to ensure that the regular payment process provides the essential elements of control over the disbursement of Agency funds, it is necessary to examine some claims in a more detailed manner. The system which does this is the Post Payment Audit regime.

The Post Payment Audit regime uses statistical sampling to identify which claims will be audited. The objective is to sample sufficient claims so that we can provide a conclusion on whether or not the payment process can be relied upon.

The sample is compiled monthly and is taken from a list of claims paid by the Agency from the data warehouse which stores the Agency's financial data. Computer assisted audit techniques are used to identify the sample from the complete information in the data warehouse. The resulting sample is a monetary dollar value sample, thus biased toward higher dollar value claims. The sample is provided to each region, which is required to complete an audit of the supporting documentation, verify the terms and conditions of the contract for the project, and complete other steeps which firmly address the validity of the claim. Once the claim is audited, the results are posted directly to the Post Payment Audit intranet site.

APPENDIX B – Regional PPA Completion Statistics

April 1, 2001 to October 31, 2001

Region	No. of Claims selected for PPA	No. of Claims Audited	Percentage of Audits Completed
Cape Breton	24	24	100
Prince Edward Island	21	18	85.7
Nova Scotia	29	11	37.9
New Brunswick	41	32	78
Newfoundland	20	7	35
Head Office	6	2	33.3
Total Agency	**141**	**94**	**66.6**

APPENDIX C – 2001-2002 ADVANCE Statistics

April – October 2001

Region	Total Payments Selected for PPA	No. of which are Advances	% of Total Payments selected which are Advances
Cape Breton	24	9	37.5
Head Office	6	3	50.0
New Brunswick	41	4`	9.8
Newfoundland	20	11	55.0
Nova Scotia	29	14	48.3
Prince Edward Island	21	4	19.0
Total Agency	**141**	**45**	**31.9**

APPENDIX D – 2000-2001 - Advance Statistics

April 2000 – March 2001

Region	Number of Advances	Total Number of Claims	Percentage of Advances Given
Cape Breton	9	25	36.0
Prince Edward Island	9	52	17.3
Nova Scotia	11	41	26.8
New Brunswick	3	76	0.4
Newfoundland	22	57	38.6
Head Office	3	13	23.1
Totals	**57**	**264**	**21.6**

Post Payment Audit Process

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